

C-1. Docket Number: RM05-23-000

Statement of Chairman Joseph T. Kelliher on Gas Storage Pricing Reform December 15, 2005

This Notice of Proposed Rulemaking (NOPR) would reform Commission pricing policies for natural gas storage facilities in order to encourage greater investment in storage facilities. The Commission believes that expansion of storage capacity may help reduce volatility in natural gas prices. The goal is clear: reduce volatility in gas prices, by encouraging expansion in gas storage capacity.

Natural gas storage capacity has remained relatively static for many years, while demand has increased sharply. Since 1988, gas storage capacity has expanded only 1.4 percent, while demand has risen 24 percent. Significantly, the volatility of gas prices has risen sharply during this period. One possible cause of greater volatility in gas prices is inadequate gas storage capacity.

This order is one of the Commission's responses to a winter of record high natural gas prices. We have improved our ability to detect market manipulation by entering into a Memorandum of Understanding with the Commodity Futures Trading Commission. We have issued anti-manipulation proposed rules. We have authorized more efficient use of our existing infrastructure by acting quickly on emergency filings. We have acted to speed recovery from the hurricanes by expediting gas infrastructure construction.

Today, we act to reduce gas price volatility by encouraging expansions in storage capacity. Our action could not come at a better time.

This NOPR would reform gas storage pricing in two ways. First, it would reform the Commission's market power analysis to better reflect the competitive alternatives to storage. In particular, the NOPR would expand the product market to include close substitutes for gas storage services, such as available pipeline capacity, local gas production, and LNG imports. In short, instead of treating gas in storage as a discrete product, the Commission will recognize that gas in storage competes with other gas that can be delivered to the same geographic market.

These changes reflect the economic realities of gas storage providers. Currently, gas storage providers effectively compete with other gas supplies, whether from pipeline sales, local production, or LNG imports. The reality is that gas in storage currently competes with other gas. It is not theory, but reality. It is only appropriate that that reality be reflected in the Commission's analysis.

The order also would implement the new section 4(f) of the Energy Policy Act of 2005 (EPAAct), which authorized the Commission to permit market-based rates for new gas storage facilities, even if the provider is unable to show it lacks market power, if the Commission determines that market-based rates are in the public interest and necessary to encourage needed storage infrastructure and that customers are adequately protected.

It is important to recognize that this EAct authority is effective immediately. There is no requirement that the Commission issue rules to implement this provision, but we do so to clarify our approach on any future filings for market-based rates under the new EAct provision.

I want to emphasize that EAct authorizes the Commission to allow market-based rates for a gas storage provider – even if it has market power – only if certain findings are made. Market-based rates have to be in the public interest and necessary to encourage needed infrastructure. Further, customers must be adequately protected.

The NOPR proposes a number of ways to protect customers. For example, an applicant could propose measures to prevent withholding, by requiring the storage operator to sell or make available to the market all of its capacity. The burden rests with the applicant to prove to the Commission that customers are protected.

All in all, this order clearly benefits consumers, by reducing price volatility.

I want to note that this proposed rule provides an alternative approach. A prospective developer of a new storage facility need not go through the modified market power analysis, and may make an EAct filing directly.

Gas storage pricing reform is something the Commission has been considering for some time. It is one of my top priorities as Chairman, something I announced on my first day in office. The state of the gas industry conference in October 2004 examined this very issue. But the fact that Congress gave us this new authority adds momentum to our efforts. EAct shows that Congress recognizes the relationship between gas storage capacity and price volatility, and Congress arrived at the same solution: reform gas storage pricing.

I respect the judgment of Congress and agree with the policy goal. We are moving swiftly to implement our new EAct authority.

I support the order.